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No. 92-873

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1992

RHINE REINSURANCE CO., LTD.; AMERICAN INTERNATIONAL GROUP, INC.; THE HOME INSURANCE COMPANY; NATIONWIDE MUTUAL INSURANCE COMPANY; RESOLUTE REINSURANCE COMPANY AND ARKWRIGHT MUTUAL INSURANCE COMPANY (AS SUCCESSOR IN INTEREST TO PHILADELPHIA MANUFACTURERS MUTUAL INSURANCE COMPANY),

Petitioners,

vs.

CYNTHIA MALESKI, Acting Insurance Commissioner of the Commonwealth of Pennsylvania as Rehabilitator of the Mutual Fire, Marine & Inland Insurance Company *et al.*,

Respondents.

Petition for a Writ of Certiorari to the Supreme Court of Pennsylvania

SUPPLEMENTAL BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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LIST OF PARTIES

The Petitioners include Rhine Reinsurance Co., Ltd., American International Group, Inc., The Home Insurance Company, Nationwide Mutual Insurance Company, Resolute Reinsurance Company, and Arkwright Mutual Insurance Company (as successors in interest to Philadelphia Manufacturers Mutual Insurance Company).[1] Other parties to the case include: American Centennial Insurance Co., American Financial Corp., Atlantic Mutual Fire Insurance Co., Crum and Forster, European General Reinsurance Company of Zurich, Excess and Casualty Reinsurance Association, Gerling Global Insurance Corp., The Hartford Insurance Group, Heddington Insurance, Highlands Insurance Co., Imperial Casualty and Indemnity Co., Lincoln

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1. The parent companies of Rhine Reinsurance Co. Ltd. include the Baloise Insurance Co. Ltd., Berner Allgemeine Holdinggeselischaft, Patria Life Insurance Co., and Limmat Insurance Co. Ltd.

Starr International Co., Inc., The Starr Foundation, and C. V. Starr & Co. have an ownership interest in The American International Group, Inc. Its non-wholly owned subsidiaries include INTASCO Holdings Ltd., China America Insurance Co. Ltd., China America International Insurance Co. Ltd., General Environmental Management Co., Venture Enterprises Ltd., Specialty Enterprises Ltd., American International Company Ltd., AIG Financial Products Corp., Tincino Societa d'Assicurazioni Sulla Vita, Expert Network Inc., The Phillipine American Life Insurance Co., AIG Life Insurance Co., and Trace Network International Ltd.

Home Holdings, Inc. is the parent company of The Home Insurance Company.

Nationwide Cash Management is a non-wholly owned subsidiary of Nationwide Mutual Insurance Company.

Resolute Group, Inc. is the parent company of Resolute Reinsurance Company. GEICO Corporation is the parent of Resolute Group, Inc.

F.M. Insurance Company Ltd. and Factory Mutual Engineering Corporation are non-wholly owned subsidiaries of Arkwright Mutual Insurance Company.

Insurance Co., Maiden Lane Insurance Co., Michigan Mutual Insurance Co., Mid-Continent Casualty Co., Monroe Guarantee Insurance Co.,Mutual Marine Offices, Inc., North Star Mutual Insurance Co., Northwestern National Casualty Co., Norwich Union Fire Insurance Society, Ltd., Old Republic, Pennsylvania National Insurance Companies, Royal Insurance Companies, Royal Insurance (UK), Ltd., Safety Mutual Casualty Corp., Saskatchewan Government Insurance, Scottish & York International Insurance Group, South Central Insurance Co., Sphere Drake Underwriting Management, Ltd., Utica Mutual Insurance Co., H. S. Weavers Agencies, Ltd., Willis Faber (Underwriting Management), Ltd., Wausau Insurance Companies, The Republic Insurance Group, NAIC Reinsurance Corporation, Winterthur Reinsurance Corp. of America f/k/a in the U.S. as Winterthur Swiss Insurance Co., U.S. Branch, GTE Reinsurance Co., Ltd., Christiania General Insurance Corp. of New York, Reinsurance Corp. of New York, Evanston Insurance Company, RLI Insurance Company, Pepsi-Cola Bottling Co. of Charlotte, Inc., Pennsylvania Insurance Guaranty Association, Allstate Insurance Co., Fireman's Fund Insurance Co., Interstate Fire & Casualty Co., and Committee of Policyholders.

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This supplemental brief is filed pursuant to Supreme Court Rule 15.7, in order to call the Court's attention to a new decision not available when Petitioners' Petition for a Writ of Certiorari ("Petition") was filed. In their Petition, Petitioners cited a decision of the California Court of Appeals, *Prudential Reinsurance Company v. The Superior Court*, 6 Cal. App. 4th 275, 256 Cal. Rptr. 386 (1990), *aff'd slip op.* No. SO14036, 1992 WL 347585 (Cal. 11/30/92), which involved the issue of reinsurers' rights of offset against an insolvent insurer, Mission Insurance Company ("Mission"). Petitioners did so in support of their argument that, under this Court's decision in *Energy Reserves Group, Inc. v. Kansas Power and Light Company*, 495 U.S. 400 (1983), protecting the interests of policyholders is not a public purpose sufficiently "significant and legitimate" to permit an insolvent insurer to repudiate its contractual setoff obligations with its reinsurers. Petition at 18, n. 12. After the Petition was filed, the California Supreme Court affirmed the Court of Appeals decision. Slip op. No. SO14036, 1992 WL 347585 (Cal. 11/30/92).

In doing so, the California Supreme Court ruled that enforcing the reinsurers' rights of setoff was compelled by their contracts with Mission and state law, and therefore outweighed any asserted public interest in protecting policyholders or another general class of Mission creditors, even if "allowance of a setoff permits reinsurers to obtain complete satisfaction of the debt they are owed, while Mission policyholders are relegated to partial satisfaction only." *Prudential Reinsurance*, slip op. at [illegible]. The Court rejected the argument that "the insolvency statutes were adopted to protect the interests of policyholders and the public in general and setoff would abrogate that protection," *Prudential Reinsurance*, slip op. at 16, finding instead — as Petitioners have argued — that to disallow setoff "would not only subvert clear legislative intent, but would also lead to an increased cost of insurance for the consumer, because offsetting an insurer's debts spreads the risk incurred by the insurer and often allows smaller

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insurers to remain in business." *Prudential Reinsurance*, slip op. at 2; *cf.* Petition at 8-9 and n. 7.

The California Supreme Court's decision in *Prudential Reinsurance* is in conflict with the decision of the Pennsylvania Supreme Court that is the subject of the Petition, thereby providing a basis additional to that set forth in the Petition for granting the requested Writ of Certiorari. The Pennsylvania Supreme Court ruled that the Contract Clause did not require it to modify or amend Mutual Fire's Plan of Rehabilitation ("Plan") even though the Plan ignored the setoff clauses found in Petitioners' agreements with Mutual Fire. The Pennsylvania Court found that the Plan created no "substantial impairment" of the agreements, and further that any impairment that might exist was outweighed by the Commonwealth's "significant interest" in regulating the fiscal affairs of insurers. Petition at 16a, n. 4. The Pennsylvania Court made this determination in spite of a Pennsylvania state statute that requires the setoff of mutual debts or mutual credits between an insurer in rehabilitation and its creditors, except of premiums owed the insurer. 40 P.S. § 221.32. *See* Petition at 11.

In marked contrast to the approach taken by the Supreme Court of Pennsylvania, the California Supreme Court acknowledged that the contracts between an insolvent insurer and its reinsurers allow for offset by either party of "any and all reinsurance debts owed by or to them." Slip op. at 3. It then noted that, under the California equivalent of 40 P.S. § 221.32, these contractual obligations must survive the insolvency of the insurer provided the debts to be offset are "mutual." Slip op. at 4; Cal. Ins. Code, Art. XIV, § 1031. The California Court concluded that "the reciprocal reinsurance contracts at issue here created 'mutual credits and debts'" that must be offset pursuant to the relevant statute. Slip op. at 2.

The decisions of the California and Pennsylvania Supreme Courts cannot be reconciled. Had the Pennsylvania court accepted,

as did the California court, the plain meaning of the Petitioners' contracts with Mutual Fire and enforced, as did the California court, the statutory provision mandating setoff, it would not have so blithely dismissed Petitioners' Contract Clause arguments. To be consistent with *Prudential Reinsurance*, the Pennsylvania Supreme Court would have been obliged to determine that the Plan substantially impairs Petitioners' contractual rights. It would also have had to conclude that the Plan serves no "significant and legitimate public purpose," but rather frustrates the important general goal of promoting security among reinsurers and spreading risk.[1]

The *Prudential Reinsurance* case makes clear that Petitioners' rights under the Contract Clause cannot properly be analyzed without considering their agreements with Mutual Fire or the provision of state law mandating setoff. A similar conclusion is reached by applying to Petitioners' claims this Court's decision in *Energy Reserves*. Accordingly, this Court should grant the Petitioners' Petition in order to correct the Pennsylvania Supreme

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1. The California Supreme Court in *Prudential Reinsurance* apparently considered the Pennsylvania Supreme Court decision in the present case, observing in a footnote that the facts before the Pennsylvania court were distinguishable from those in *Prudential Reinsurance* because 40 P.S. § 221.32(a)(4), unlike Section 1031 of the California Insurance Code, "expressly prohibits reinsurer setoff of premium obligations." Slip op. at 9, n. 4. As noted in the Petition, Petitioners believe that 40 P.S. § 221.32(a)(4) violates the Contract Clause and should be ruled unconstitutional.. Petition at 12, n. 10. They also believe, based upon the language of this provision and its context, that it does not compel a different result from that reached in *Prudential Reinsurance*. In any event, however, it is clear that had the Pennsylvania Supreme Court followed the reasoning of the Court in *Prudential Reinsurance*, it would have reached and decided the issue of the constitutionality of § 221.32(a)(4) and its applicability to this case. The Writ of Certiorari should be granted so that this Court may determine whether the Pennsylvania Supreme Court should have considered this issue instead of ignoring it.

Court's failure to act consistently with the Court's directives in evaluating claims under the Contract Clause.

Respectfully submitted,

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